LISA I. CARTEEN, Bar No. 204764
BAKER & HOSTETLER LLP
12100 Wilshire Boulevard, 15th Floor
Los Angeles, California 90025-7120
Telephone: 310.820.8800
Facsimile: 310.820.8859
Email: lcarteen@bakerlaw.com

BRUCE O. BAUMGARTNER, Bar No. 0025701 (*Pro Hac Vice*)
ROBIN E. HARVEY, Bar No. 0014183 (*Pro Hac Vice*)
BAKER & HOSTETLER LLP
312 Walnut Street, Suite 3200
Cincinnati, Ohio 45202-4072
Telephone: 513.929.3400
Facsimile: 513.929.0303
Email: bbaumgartner@bakerlaw.com
rharvey@bakerlaw.com

LEE H. SIMOWITZ, Bar No. 185728 (*Pro Hac Vice*)
BAKER & HOSTETLER LLP
1050 Connecticut Avenue, NW, Suite 1100
Washington, DC 20036-5304
Telephone: 202.861.1500
Facsimile: 202.861.1783
Email: lsimowitz@bakerlaw.com

Attorneys for Defendants
GANZ, INC. and GANZ U.S.A., LLC

UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

NUTS FOR CANDY, a Sole Proprietorship, individually and on behalf of all others similarly situated,

Plaintiff,

v.

GANZ, INC. and GANZ U.S.A., LLC,

Defendants.

Case No. CV 08-2873 JSW

DEFENDANTS' NOTICE OF MOTION AND MOTION TO DISMISS PLAINTIFF'S COMPLAINT

Date: November 7, 2008
Time: 9:00 a.m.
Judge: Hon. Jeffrey S. White
Ctrm.: Courtroom 2, 17th Floor

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NOTICE OF MOTION AND MOTION

TO ALL PARTIES AND THEIR COUNSEL OF RECORD:

PLEASE TAKE NOTICE that on November 7, 2008 at 9:00 a.m. or as soon as the matter may be heard before the Honorable Jeffrey S. White of the United States District Court, Northern District of California, San Francisco Division, 450 Golden Gate Avenue, 17th Floor, San Francisco, California 94102, in Courtroom 2, Defendants Ganz, Inc. and Ganz U.S.A., LLC will and hereby do move the Court for an order dismissing Plaintiff's Complaint.

This motion is brought pursuant to Federal Rule of Civil Procedure 12(b)(6) on the grounds that Plaintiff has failed to state a claim under the antitrust laws and Plaintiff's Complaint should be dismissed.

This motion is based on this Notice, the attached Memorandum of Points and Authorities, all pleadings and papers on file in this action, and upon such other documentary and oral evidence as may be presented to the Court at the time of the hearing on this Motion.

Dated: August 4, 2008

Respectfully submitted,

BAKER & HOSTETLER LLP
LISA I. CARTEEN

/s/ Lisa I. Carteen
Lisa I. Carteen

Attorneys for Defendants
GANZ, INC. and GANZ U.S.A., LLC

MEMORANDUM OF POINTS AND AUTHORITIES

I. INTRODUCTION

Plaintiff, a sole proprietorship selling chocolates, candy, toys, gifts and ice cream, filed a legally baseless Complaint asserting Defendants imposed on it and other alleged members of a purported class a *per se* unlawful tying arrangement in violation of the Sherman Act, 15 U.S.C. Sec. 1, and the Clayton Act, 15 U.S.C. Sec. 14. Plaintiff claims that Defendants adopted and implemented a "co-order" policy and Loyalty Program requiring some of Defendants' customers to purchase any of Defendants' other products "unrelated to Webkinz" when they placed initial orders for Defendants' popular Webkinz products. (Compl. ¶ 2.) Plaintiff's incurably defective Complaint fails to state a claim under controlling U.S. Supreme Court and Ninth Circuit antitrust decisions.

II. SUMMARY OF ARGUMENT

Tying arrangements are unlawful only if they reduce competition in the market for the tied product by using market power in the market for the tying product. The Complaint here fails on both scores. First, illegal tying arrangements must produce an anticompetitive effect in the market for the tied product. But the Complaint does not allege even a tied product market, let alone an anticompetitive effect in that market. Moreover, the tied products cannot be a market because they comprise an unidentified mass of products whose only characteristics are that Defendants sell them, and they are not Webkinz – the alleged tying product.

Second, the Complaint fails to allege any facts that could support the conclusion that Webkinz - a menagerie of toy monkeys, lions, dogs and other creatures, linked to an interactive Web site - possesses market power in a relevant tying product market, the essential ingredient of any *per se* tying claim. The skeletal and conclusory facts alleged in the Complaint do not warrant a finding of market power, particularly in view of the Ninth Circuit's recent and controlling decision in *Rick-Mik Enterprises, Inc. v. Equilon Enterprises, LLC*, No. 06-55937, 2008 U.S. App. LEXIS 14761 (9th Cir. July 11, 2008). Indeed, the Complaint admits that the nation's largest toy companies sell competing products, and fails to allege any barriers that could prevent other companies from offering additional competitive products.

The Complaint's myriad flaws do not simply reflect a failure of pleading; rather, they betray the absence of any plausible facts that could support an antitrust claim, requiring dismissal of the Complaint in its entirety.

III. ALLEGATIONS OF THE COMPLAINT

Defendants Ganz, Inc., a Delaware Corporation, and its related company Ganz U.S.A., LLC (collectively referred to as "Ganz"), "creat[e] and sell[] toys" in the United States. Compl. ¶ 15. Those toys include Webkinz, a "highly popular" line of plush stuffed animals. Compl. ¶ 3. Each Webkinz comes with a code that enables the user to unlock a Web site that offers online games and other activities, allowing the user to care for a virtual pet by earning points from playing games. *Id.*

Webkinz allegedly competes in a "relevant product market" defined as "the United States market for toys combined with online gaming." Compl. ¶ 37. The Complaint alleges that Webkinz "enjoys a dominant position" in this market. Compl. ¶ 38. However, according to the Complaint itself, at least four other products sold by major toy companies compete in this market: Hasbro's Littlest Pet Shop VIPs, Shining Stars, Mattel's U.B. Funkeys, and the Be-Bratz doll. Compl. ¶¶ 30, 32. The Complaint does not allege any barriers impeding entry into the alleged market, nor could such an allegation be made, given the entry of major competitors.

While acknowledging the existence of competing products, the Complaint makes no allegation regarding Ganz's share of the alleged market. Instead, Plaintiff Nuts for Candy (a sole proprietorship that sells chocolates, candy, toys, gifts, and ice cream) (Compl. ¶ 14) bases its claim that Webkinz has a "dominant position" on allegations regarding Webkinz's showing in children's "coolest toy" surveys, raw sales data for Webkinz only (estimated $100 million sales "by late 2007"), "unique" visits to the Webkinz Web site, frequency of web searches, and average length of web visits. Compl. ¶¶ 38-41. Without similar data for competing products, Nuts for Candy has somehow calculated that "Webkinz's share of unique visitors to online gaming sites combined with a toy is approximately 80%." Compl. ¶ 41.

Before allowing a retailer to order Webkinz for the first time, Ganz requires the new retailer to order at least $1,000 of Ganz "core line" products and then submit an application to

order Webkinz. Compl. ¶ 4. The "core line" is defined only as "Ganz products unrelated to Webkinz, including lip gloss, magnets, and stuffed and rubber animals." Compl. ¶ 2.

Nuts for Candy alleges that Ganz's retailer requirements constitute a *per se* unlawful tying arrangement in violation of Section 1 of the Sherman Act, 15 U.S.C. § 1, and Section 3 of the Clayton Act, 15 U.S.C. § 14. Compl. ¶ 61. The tying product is Webkinz and the tied product is Ganz's "core line," i.e., "Ganz products unrelated to Webkinz." Compl. ¶ 2. While the alleged "relevant product market" – by which Nuts for Candy apparently means the tying product market – is "the United States market for toys combined with online gaming," Compl. ¶ 37, the Complaint makes no allegation regarding the market in which the *tied* products compete.

The Complaint further alleges that Ganz's "tying arrangement has been successful" in that "many Class members would not have ordered the tied Ganz products, or would have ordered smaller amounts than Ganz forced them to order." Compl. ¶ 56. The only monetary injury alleged by Nuts for Candy is the "forced" purchase of $1,035 in unwanted "core line" products so that Nuts for Candy could order Webkinz. Compl. ¶ 14. Nuts for Candy does not allege monetary injury as a result of any increase in price, restriction in supply, or diminution in quality of these so-called "tied Ganz products." The Complaint neither identifies other competitors in this undefined tied product market nor alleges facts illustrating the alleged foreclosure of commerce or harm to competition in that market.

IV. ARGUMENT

A. An Antitrust Complaint Must Provide A Factual Basis For A Claim

The Ninth Circuit has held that "in antitrust matters, '[f]actual allegations must be enough to raise a right to relief above the speculative level[.]'" *Rick-Mik Enterprises, Inc.*, 2008 U.S. App. LEXIS 14761 at *13 (9th Cir. July 11, 2008) (quoting *Bell Atlantic Corp. v. Twombly*, 127 S.Ct. 1955, 1965 (2007)). As *Twombly* held, "a plaintiff's obligation to provide the grounds of his entitlement to relief requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do." 127 S.Ct. at 1964-65 (internal punctuation omitted); *see also Papasan v. Allain*, 478 U.S. 265, 286 (1986) (court "not bound to accept as true a legal conclusion couched as a factual allegation").

As the Ninth Circuit observed in *Rick-Mik Enterprises, Inc.*:

> In *Twombly*, at least in antitrust matters, the Supreme Court "retired" the familiar language derived from *Conley v. Gibson*, 355 U.S. 41, 45-46 . . . , which provided "the accepted rule that a complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." 127 S.Ct. at 1968 (quoting *Conley*). *Twombly* opined that the "no set of facts" language "has earned its retirement" and "is best forgotten[.]" *Id.* at 1969. Thus, "[a]t least for the purposes of adequate pleading in antitrust cases, the Court specifically abrogated the usual 'notice pleading' rule[.]" *Kendall v. Visa U.S.A., Inc.*, 518 F.3d 1042, 1047 n.5 (9th Cir. 2008).

2008 U.S. App. LEXIS 14761 at **13-14. Rejecting *Conley's* "no set of facts" language, *Twombly* said that such language "can be read in isolation as saying that any statement revealing the theory of the claim will suffice unless its factual impossibility may be shown from the face of the pleadings." 127 S.Ct. at 1968. Such a lenient standard is unacceptable: "[I]t is one thing to be cautious before dismissing an antitrust complaint in advance of discovery, but quite another to forget that proceeding to antitrust discovery can be expensive." *Id*. at 1966-67 (citation omitted). Where, as here, "the allegations in a complaint, however true, could not raise a claim of entitlement to relief, 'this basic deficiency should . . . be exposed at the point of minimum expenditure of time and money by the parties and the court.'" *Id.* at 1966 (citation omitted).

The Ninth Circuit also has recognized that "[i]ndispensable to any [Sherman Act] section 1 claim is an allegation that *competition* has been injured rather than merely competitors." *Rutman Wine Co. v. E. & J. Gallo Winery*, 829 F.2d 729, 734 (9th Cir. 1987). In *Rutman*, the court affirmed the dismissal of an antitrust action, holding that "[w]hile appellant clearly pleads injury to itself, its conclusion that competition has been harmed thereby does not follow." *Id.* The court added: "[I]f the facts do not at least outline or adumbrate a violation of the Sherman Act, the plaintiffs will get nowhere merely by dressing them up in the language of antitrust." *Id.* at 736 (internal quotations and citations omitted).

Nuts for Candy's allegations must also be evaluated in light of the Supreme Court's recent change in approach to tying claims: "Over the years . . . this Court's strong disapproval of tying arrangements has substantially diminished." *Illinois Tool Works Inc. v. Indep. Ink, Inc.*, 547 U.S. 28, 35 (2006). Rather than relying on a presumption that a patent confers market power on the

patentee, the Court held that "*in all cases* involving a tying arrangement, the plaintiff must prove that the defendant has market power in the tying product." *Id.* at 46 (emphasis added). The Court expressed strong reluctance to hold tying arrangements per se unlawful, recognizing that "[m]any tying arrangements . . . are fully consistent with a free, competitive market." *Id.* at 45.

These Supreme Court opinions expose two fundamental deficiencies in Nuts for Candy's Complaint. First, Nuts for Candy fails even to allege a market for the supposedly tied products, let alone allege facts sufficient to show the requisite harm to competition in such a market. Second, Nuts for Candy fails to allege that Ganz has market power in the tying product. In fact, the Complaint alleges facts that establish *absence* of market power: that major toy companies, including Mattel and Hasbro, sell products directly competitive with Webkinz, and no barriers impede others from offering similar products in this crowded competitive landscape.

B. The Complaint Fails To Allege An Anticompetitive Effect In A Market For A Tied Product

The potential harm in a tying arrangement lies in use of market power in one market – the market for the tying product – to produce an anticompetitive effect in the market for a second, or tied, product. Without pleading and proof of an anticompetitive effect in the tied product market, there can be no unlawful tying. Yet the Complaint does not even allege the *existence* of a tied product market, let alone define that market or allege harm to competition there. Instead, the Complaint refers to a hodge-podge of unidentified products whose only common feature is that they are sold by Ganz, and are not Webkinz, i.e., "Ganz products unrelated to Webkinz, including lip gloss, magnets, and stuffed and rubber animals." Compl., ¶ 2.

1. The Vice Of A Tying Arrangement Lies In Its Effect On The Tied Product Market

The basis for condemning tying arrangements as a violation of the Sherman Act lies in their impact on competition in the *tied* product market. In *Illinois Tool Works*, the Supreme Court summarized more than 90 years of tying cases with this observation:

> [T]he justification for the challenge rested on either an assumption or a showing that the defendant's position of power in the market for the tying product was being used *to restrain competition in the market for the tied product*.

547 U.S. at 34 (emphasis added); *see also Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2,

12 (1984) (tying arrangement violates Sherman Act because "competition on the merits in the market for the tied item is restrained").

The Ninth Circuit has reiterated this principle even more recently:

> A tying arrangement is a device used by a seller with market power in one product market to *extend its market power to a distinct product market*. . . . Tying arrangements are forbidden on the theory that, if the seller has market power over the tying product, the seller can leverage this market power through tying arrangements *to exclude other sellers of the tied product*.

Cascade Health Solutions v. PeaceHealth, 515 F.3d 883, 912 (9th Cir. 2008) (emphases added); *see also Rick-Mik Enterprises, Inc.*, 2008 U.S. App. LEXIS 14761, at *16 (in tying arrangements, "[t]he injury is reduced competition in the market for the tied product"); *Siegel v. Chicken Delight, Inc.,* 448 F.2d 43, 47 (9th Cir. 1971) ("[t]he hallmark of a tie-in is that it denies competitors free access to the tied product market").

The vice of a tying arrangement thus lies not in the requirement, by itself, that a customer purchase unwanted products, but in the reduction of *competition* in the market for those unwanted products. "[W]hen a purchaser is 'forced' to buy a product he would not have otherwise bought even from another seller in the tied product market, there can be no adverse impact on competition because no portion of the market which would otherwise have been available to other sellers has been foreclosed." *Jefferson Parish*, 466 U.S. at 16.

2. To Establish An Unlawful Tying Arrangement, Plaintiff Must Plead And Prove An Effect On Competition In The Tied Product Market

To establish that a tying arrangement is illegal *per se*, a plaintiff must prove (i) two distinct products or services; (ii) a sale or agreement to sell the tying product conditioned upon the purchase of the tied product; (iii) market power in the relevant market for the tying product; and (iv) that the tied product involves a "not insubstantial" amount of interstate commerce. *Jefferson Parish*, 466 U.S. at 12-18. This means that to state a claim for tying, a plaintiff must allege "two distinct products and two distinct markets." *Catch Curve, Inc. v. Venali, Inc.*, 519 F. Supp. 2d 1028, 1039 (C.D. Cal. 2007).

In addition to these elements, the Ninth Circuit, as well as other circuits, require the plaintiff to show a "pernicious effect" on competition in the tied product market. *In re eBay*

Seller Antitrust Litig., 545 F. Supp. 2d 1027, 1033-34 (N.D. Cal. 2008) (citing *Siegel*, 448 F.2d at 47); *see also United Farmers Agents Ass'n, Inc. v. Farmers Ins. Exch.*, 89 F.3d 233, 235-36, n. 2 (5th Cir. 1996) (requiring anticompetitive effect on tied market); *Power Test Petroleum Distribs., Inc. v. Calcu Gas, Inc.*, 754 F.2d 91, 96 (2d Cir. 1985) (same).

In *eBay,* the tying claim was dismissed because "Plaintiffs have not alleged sufficiently that a tie actually caused harm to competitors in the [tied product] market." 545 F. Supp. 2d at 1034. Absence of harm in the tied product market has resulted in rejection of tying claims in other courts as well. *See, e.g., CTUnify, Inc. v. Nortel Networks, Inc.*, 115 Fed. Appx. 831, 836 (6th Cir. 2004) (dismissing tying claim where plaintiff "has not concretely alleged any anticompetitive effect that the defendants' tying agreement has had on the tied market"); *Driskill v. Dallas Cowboys Football Club, Inc.*, 498 F.2d 321, 323 (5th Cir. 1974) (affirming summary judgment where defendant's "complete monopoly in the tied market" prevented adverse effect on competition); *United Magazine Co. v. Murdoch Magazines Distrib., Inc.*, 146 F. Supp. 2d 385, 399 (S.D.N.Y. 2001) (dismissing tying claim where "there are no competing distributors of the tied products" because "there can be no anticompetitive effects in the tied markets").

To prevail on an antitrust claim arising out of an unlawful tying arrangement, a plaintiff therefore must plead and prove two distinct product markets for the tying and tied products. A plaintiff also must plead and prove an anticompetitive effect in the market for the tied product. As shown below, Nuts for Candy has not even attempted either allegation.

3. The Complaint Does Not And Cannot Allege A Tied Product Market

According to the Complaint, "the relevant product market" should be defined as "the United States market for toys combined with online gaming." Compl. ¶ 37. Regardless of the adequacy or inadequacy of this alleged market as a *tying* product market, the Complaint fails to state a claim because it does not allege, even purportedly, a *tied* product market. While the Complaint refers in passing to a second market as "the market in which the tied products compete" (Compl. ¶ 28), Nuts for Candy makes no attempt to define this market.

In *Catch Curve*, the plaintiff's tying allegation was dismissed for failure to "allege two distinct products and two distinct markets." 519 F. Supp. 2d at 1039. In dismissing the allegation,

the court held that it could not guess at alleged products or markets that were not defined in the complaint. *Id.* Here, the "tied Ganz products" are defined in the Complaint merely as "products from Ganz's 'core line.'" Compl., ¶ 2. Ganz's "core line," in turn, is identified only as something that "consists of Ganz products unrelated to Webkinz, including lip gloss, magnets, and stuffed and rubber animals." *Id.* Otherwise put, the "tied Ganz products" appear to be everything else that Ganz happens to sell at any given moment.

It cannot be determined from the Complaint which, if any, Ganz products besides "lip gloss, magnets, and stuffed and rubber animals" are included in the definition of the tied product. Nor can it be determined if all Ganz "lip gloss, magnets, and stuffed and rubber animals" are considered tied products, since Webkinz – the tying product – is itself a "line of plush stuffed animals," thus making the Complaint's attempt to describe the "tied products" circular. Compl. ¶ 3.

Even to the extent that the identity of the alleged tied products can be determined, however, the Complaint lacks any attempt to define the market in which those tied products compete. Virtually any conceivable tied market definition Nuts for Candy might allege would undermine its claims. The tied market cannot be Ganz "core line" products, as single-seller product markets are routinely rejected. *See, e.g., Green Country Food Mkt., Inc. v. Bottling Group, LLC*, 371 F.3d 1275, 1283 (10th Cir. 2004) (Pepsi products not relevant market); *Elliott v. United Ctr.*, 126 F.3d 1003, 1004-06 (7th Cir. 1997) (single arena food sales not a relevant market); *Town Sound & Custom Tops, Inc. v. Chrysler Motors Corp.*, 959 F.2d 468, 480 (3d Cir. 1992) (en banc) (Chrysler cars not relevant market; "[e]xcept in rare circumstances, courts reject market definitions consisting of one supplier's products where other brands compete").

Nor can the tied market be all suppliers' "lip gloss, magnets, and stuffed and rubber animals," because a market that includes all stuffed animals necessarily includes Webkinz, violating the requirement that the tying and tied product markets be distinct. *See Jefferson Parish,* 466 U.S. at 18; *Catch Curve,* 519 F. Supp. 2d at 1039. Surely the tied market is not all "lip gloss, magnets, and stuffed and rubber animals" *except* "toys with online gaming" (the alleged tying product market), for what principled basis justifies placing stuffed animals without

an online component in a separate market from Webkinz, but in the same market as lip gloss?

As Nuts for Candy itself recognizes, a product market is defined by "the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it." Compl., ¶ 29 (emphasis removed). Thus, a product market is typically defined to include the set of goods or services that qualify as economic substitutes because they enjoy reasonable interchangeability of use and cross-elasticity of demand. *Thurman Indus., Inc. v. Pay 'N Pak Stores, Inc.*, 875 F.2d 1369, 1374 (9th Cir. 1989); *see also Brown Shoe Co. v. United States*, 370 U.S. 294, 325 (1962) (product market defined by "reasonable interchangeability of use" or "cross-elasticity of demand between the product itself and substitutes for it").

Any attempt to define a tied product market that includes a wide variety of products sold by Ganz, but excludes Webkinz, will inevitably contravene any notion of either reasonable interchangeability of use or cross-elasticity of demand. Lip gloss and magnets, for example, are not interchangeable in their use, and surely there is no cross-elasticity in the demand for these two products, i.e., an increase in the price of lip gloss will not cause consumers to buy more magnets. They, along with the other named and unnamed items constituting the so-called "tied Ganz products," are lumped into a single market for two reasons: (i) Ganz sells them and (ii) they are not Webkinz. Defining a tied product market as encompassing all products sold by the defendant except the tying product, however, bears no relationship to economic substitutability.

Because Nuts for Candy has failed to allege the tied products with any specificity, failed to allege any market in which the tied products compete, and cannot allege such a tied product market within the confines of its own claim, the Complaint should be dismissed.

4. The Complaint Does Not Allege Any Harm To Competition

Nuts for Candy's omission of any definition of the tied product market – the market that is harmed in an unlawful tying arrangement – reflects the true nature of its grievance. Nuts for Candy is not complaining that portions of the undefined tied product market have been foreclosed to other competitors; indeed, it has failed to identify any other suppliers that compete in this "market." The Complaint makes clear that the alleged harm lies not in any foreclosure of competition in the unspecified tied product market, but in Nuts for Candy's allegedly "forced"

purchase of unwanted items. However, as a matter of law, "[f]orcing a buyer to purchase a product he otherwise would not have purchased is insufficient to establish the foreclosure of competition." *Reifert v. S. Cent. Wisc. MLS Corp.*, 450 F.3d 312, 318 (7th Cir. 2006). While Nuts for Candy's cost of selling Webkinz may have been increased by the alleged requirement that it purchase unwanted items, increased costs do not equate to a violation of the antitrust laws.

The Complaint is replete with references to alleged harm that have nothing to do with any foreclosure of competition in a tied product market:

- The Complaint references "monetary injury" and "wrongful profits" as a result of the "forced" purchases, but not as a result of any increase in prices or reduction in supply with respect to the "tied Ganz products." Compl., ¶ 7.
- The Complaint alleges that Ganz's conduct is "subjectively motivated by a desire to restrict competition in *the relevant market*," and that the alleged tying arrangement "has had the effect of restricting competition in the *relevant product market*." Compl., ¶ 45 (emphases added). The "relevant product market," as defined in the Complaint, is the *tying* product market – "the United States market for toys combined with online gaming." Compl., ¶ 37.
- The Complaint alleges that Ganz "adopted and implemented these policies and practices to preserve and extend its dominant position in the *relevant market*." Compl., ¶ 47 (emphasis added).

The Complaint does allege, as an afterthought, that Ganz's conduct has "had the effect of reducing the level of competition in the relevant market and in the market for the tied Ganz products" and that "Ganz's conduct has allowed it to maintain and increase its market share in those markets." Compl., ¶ 47. However, without any factual allegations as to how competition in the undefined tied product market has been reduced, or how that reduction in competition has harmed plaintiff, such conclusory allegations of anticompetitive effect are insufficient. *Les Shockley Racing v. Nat'l Hot Rod Ass'n*, 884 F.2d 504, 508 (9th Cir. 1989) ("claimant may not merely recite the bare legal conclusion that competition has been restrained"); *Rutman Wine Co.*, 829 F.2d at 734-35 (rejecting conclusory allegation that injury to plaintiff necessarily harms competition).

A tying claim requires Plaintiff to plead and prove that as a result of Ganz's conduct, competition in a second, tied product market – in which Webkinz does not compete – was reduced, and that the reduction in competition in that second market harmed Plaintiff. Nuts for Candy has alleged no tied product market, no facts supporting its conclusory allegation that competition in a tied product market was reduced, and no harm as a result of such reduced competition. In short, Nuts for Candy has not alleged an unlawful tying arrangement.

C. The Complaint Fails To Allege That Ganz Possesses Market Power In A Relevant Product Market

The Complaint must be dismissed for a second, independent reason: the Complaint fails to allege that Ganz possesses market power in a relevant product market for the *tying* product. Pleading and proof of market power in the supposed tying product is an essential element of a *per se* tying claim. The Complaint, however, fails to allege any facts from which market power can be determined or inferred. Moreover, the Complaint fails to allege entry barriers, without which there can be no market power; indeed, the Complaint affirmatively alleges that Webkinz toys compete with products introduced and sold by the world's largest toy companies.

1. The Complaint Fails To Allege That Webkinz Has Market Power

Market power in the tying product is essential to a *per se* unlawful tying arrangement. "[I]n all cases involving a tying arrangement, the plaintiff must prove that the defendant has market power in the tying product." *Illinois Tool Works Inc.*, 547 U.S. at 46. "A tying arrangement is a device used by a seller with market power in one product market to extend its market power to a distinct product market." *Cascade Health Solutions*, 515 F.3d at 912. A complaint that fails to allege market power must be dismissed. "If [the defendant] lacks market power in the [relevant] market, there can be no cognizable tying claim. . . . A failure to allege power in the relevant market is a sufficient ground to dismiss an antitrust [tying arrangement] complaint." *Rick-Mik Enterprise, Inc.*, 2008 U.S. App. LEXIS 14761, at *18.

The Complaint fails to allege *any* facts that, if proven, would support a finding of market power. The Ninth Circuit's recent decision in *Rick-Mik Enterprises* provides a roadmap to the deficiencies of the Complaint here, and to why the Complaint should be dismissed. The plaintiff

in *Rick-Mik Enterprises* also alleged a tying arrangement – that the defendant illegally used market power in gasoline franchises to coerce its franchisees to buy other services. The Ninth Circuit affirmed dismissal of the complaint because the plaintiff failed to allege market power.

> [O]ther than stating that "[Equilon] rank[s] number one in the industry in branded gasoline stations," there are no specific allegations at all as to the franchise market. The complaint alleges nothing about, for example, what percentage of gasoline franchises are Equilon's (Shell/Texaco) as compared to other franchises like Chevron, Mobil, Marathon Oil, or Union 76. There are no factual allegations as to the percentage of gasoline retail sales that are made through non-franchise outlets. There are no factual allegations regarding the amount of power or control that Equilon has over prospective franchisees. There are no factual allegations regarding the relative difficulty of a franchisee to switch franchise brands.

Rick-Mik Enterprises, Inc., 2008 U.S. App. LEXIS 14761 at *17-18.

Each of the deficiencies in the *Rick-Mik Enterprises* complaint is mirrored in this case, where the Complaint also lacks any "specific allegations at all as to the . . . market." *Id.* at *17. The Complaint here, other than the conclusory allegation that Webkinz has a "dominant position" in the supposed market for toys combined with online gaming (¶ 38), does not allege a market share for Webkinz, or any of Ganz's admitted competitors. The Complaint contains no allegation of the total size of the market, or of "the amount of power or control" (*Rick-Mik Enterprises, Inc.*, 2008 U.S. App. LEXIS 14761 at *18) that Webkinz has over its retail customers. *See also Sheridan v. Marathon Petroleum Co. LLC*, No. 07-3543, 2008 U.S. App. LEXIS 13275, at *11-12 (7th Cir. June 23, 2008) (affirming dismissal of tying complaint; "[T]he plaintiff's naked assertion of Marathon's 'appreciable economic power'—an empty phrase—cannot save the complaint.").

Instead of allegations directly addressing Ganz's supposed market power, Nuts for Candy alleges three irrelevant facts from which it hopes that market power might be inferred. (The *Rick-Mik Enterprises* plaintiff took the same "inferential" approach, which the Ninth Circuit rejected. 2008 U.S. App. LEXIS 14761 at *19-20.)

- First, the Complaint alleges that Webkinz "enjoys great popularity," because children aged six to eleven regard it as the "coolest" toy brand (girls) and the third "coolest" (boys). Compl., ¶ 38. Children's perceptions of "coolness" are, to say the least, a novel approach to proof of market power. Be that as it may, as explained below, nothing prevents such

toymakers as Mattel and Hasbro from introducing toys that can dislodge Webkinz from their current perch atop kids' "coolness" charts. "Great popularity" is not evidence of market power.

- Second, the Complaint alleges that "Webkinz sales have been high." Compl., ¶ 39. This allegation is meaningless with regard to market power, because the Complaint provides no information by which those "high" sales can be compared to sales of other toys combined with online gaming, or toys of any other type. In *Rick-Mik Enterprises*, the plaintiffs alleged high gasoline sales, and the Ninth Circuit rejected those allegations as evidence of market power. 2008 U.S. App. LEXIS 14761 at *19-20.

- Third and finally, the Complaint alleges that the Webkinz Web site had a large and growing number of unique visitors. Compl., ¶ 40. The Complaint also alleges that this information "strongly suggests that Webkinz's share of unique visitors to online gaming sites is approximately 80%." *Id.* Nothing in the Complaint, however, supports that calculation and in any event, Web site visits are not sales.

In short, the Complaint lacks any allegations that support Plaintiff's assertion that Webkinz possesses market power. In an antitrust complaint, "factual allegations must be enough to raise a right to relief above the speculative level[,]" requiring "more than labels and conclusions," or "a formulaic recitation of the elements of a cause of action[.]" *Rick-Mik Enterprises, Inc.*, 2008 U.S. App. LEXIS 14761 at *13. Nothing but "labels and conclusions" as to market power appear in Nuts for Candy's Complaint, and "[t]his failure makes every other element of the [tying] antitrust case irrelevant." *Id.* at *19 (quoting *Will v. Comprehensive Accounting Corp.*, 776 F.2d 665, 671 (7th Cir. 1985)).

2. The Complaint Alleges No Entry Barriers, And Admits The Entry Of Major Competitors

Market power is "the power to control prices or exclude competition[.]" *Paladin Assocs. v. Montana Power Co.*, 328 F.3d 1145, 1158 (9th Cir. 2003). Market power – particularly the ability to exclude competition – cannot exist, however, without entry barriers. The Complaint fails to allege the existence of entry barriers. Moreover, it is implausible that any barrier exists to the ability of competitors to offer toys combined with an interactive Web site that compete with

Webkinz. "[E]ven if [the plaintiff] has established properly the contours of the relevant market and has demonstrated that [the defendant] owns a dominant share in that market, we nevertheless conclude that [the plaintiff's] claims under Section 2 must fail because it cannot demonstrate that there are significant barriers to entry or expansion in the market it has defined." *W. Parcel Expr. v. United Parcel Serv. of Am.*, 190 F.3d 974, 975 (9th Cir. 1999). "Time after time, we have recognized this basic fact of economic life: 'A high market share, though it may ordinarily raise an inference of monopoly power, will not do so in a market with low entry barriers or other evidence of a defendant's inability to control prices or exclude competitors.'" *United States v. Syufy Enters.*, 903 F.2d 659, 664 (9th Cir. 1990) (citation omitted).

In fact, the Complaint alleges the *absence* of entry barriers: it acknowledges that some of the nation's largest toy companies have introduced and sell products that compete with Webkinz by combining a tangible toy with an interactive Web site, including Hasbro's Littlest Pet Shop VIPs (www.hasbro.com/littlestpetshop), Mattel's U.B. Funkeys (www.ubfunkeys.com), Bratz's Be-Bratz dolls (www.be-bratz.com), and Shining Stars (www.shiningstars.com). Compl., ¶¶ 30, 32. There can be no "plausible entitlement to relief" (*Twombly*, 127 S.Ct. at 1967) when the Complaint contradicts itself by alleging easy and actual entry into the market where Ganz allegedly wields market power. "When 'the complaint itself gives reasons' to doubt plaintiff's theory . . . it is not our task to resuscitate the claim but to put it to rest. Nothing prevents a plaintiff from pleading itself out of court, which is all that happened here." *NicSand, Inc. v. 3M Co.*, 507 F.3d 442, 458 (6th Cir. 2007) (en banc) (quoting *Twombly*, 127 S.Ct. at 1972).

3. The Complaint's Allegations Of Webkinz's Popularity Are Not A Substitute For The Required Allegations Of Market Position And Entry Barriers

Nuts for Candy may contend that it is relying not on Ganz's supposed market power in the conventional sense, but rather on the sheer popularity and attractiveness of Webkinz, despite Ganz's many competitors. To be sure, the Supreme Court said nearly 50 years ago in *United States v. Loew's, Inc.*, 371 U.S. 38, 45 (1962) that "[e]ven absent a showing of market dominance, the crucial economic power may be inferred from the tying product's desirability to consumers or from uniqueness in its attributes." The Supreme Court, however, disapproved

Loew's in *Illinois Tool Works* when it held that "market power in the tying product" must be proven "in *all* cases involving a tying arrangement." 547 U.S. at 46 (emphasis added).

"Uniqueness" or "desirability to consumers," in any event, is not mere popularity, which is all that the Complaint alleges regarding Webkinz. Rather, uniqueness refers to the inability of competitors to offer a competitive product, not simply their unwillingness to do so. "[T]he key question in establishing sufficient market power is whether the seller has some cost advantage not shared by its competitors which makes its competitors *unable* to provide the tying product[;] . . . a mere showing that its competitors did not want to provide the tying product is insufficient to establish an illegal tie." *Cascade Health Solutions*, 515 F.3d at 916 n.26.

The Supreme Court itself has explained that a tying product is "unique" only if competitors cannot offer it themselves. *Jefferson Parish*, 466 U.S. at 17 (tying can be found "when the seller offers a unique product that competitors are not able to offer"). *See also Will*, 776 F.2d at 672 (in a tying case, "the plaintiff must show a barrier to entry that prevents competition. If rivals may design and offer a similar package for a similar cost, there is no barrier, and without a barrier there is no market power."). Here, however, competitors not only have the ability to offer toy-plus-interactive Web site products that compete with Webkinz, but they have actually done so in large numbers, according to the allegations of the Complaint itself, thus fatally contradicting the Complaint's allegations of market power.

V. CONCLUSION

The Complaint should be dismissed pursuant to Fed. R. Civ. P. 12(b)(6).

Dated: August 4, 2008

Respectfully submitted,

BAKER & HOSTETLER LLP
LISA I. CARTEEN

/s/ Lisa I. Carteen
Lisa I. Carteen
Attorneys for Defendants
GANZ, INC. and GANZ U.S.A., LLC

UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

NUTS FOR CANDY, a Sole Proprietorship, individually and on behalf of all others similarly situated,

Plaintiff,

v.

GANZ, INC. and GANZ U.S.A., LLC,

Defendants.

Case No. CV 08-2873 JSW

[PROPOSED] ORDER GRANTING DEFENDANTS' MOTION TO DISMISS PLAINTIFF'S COMPLAINT

Date: November 7, 2008
Time: 9:00 a.m.
Judge: Hon. Jeffrey S. White
Ctrm.: Courtroom 2, 17th Floor

TO ALL PARTIES AND THEIR COUNSEL OF RECORD:

The Motion of Defendants Ganz, Inc. and Ganz U.S.A., LLC to dismiss Plaintiff Nuts for Candy's Complaint pursuant to Federal Rule of Civil Procedure 12(b)(6), on the grounds that Plaintiff has failed to state a claim under the antitrust laws, came on for hearing on November 7, 2008 at 9:00 a.m. before the Honorable Jeffrey S. White. Defendants were represented by Lee Simowitz and Bruce Baumgartner. Plaintiff was represented by Joseph Cotchett and Steven Williams.

Plaintiff's Complaint does not state a claim upon which relief can be granted, as Plaintiff has failed to state a claim for Defendants' alleged violations of Section 1 of the Sherman Act (15 U.S.C. § 1) and Section 3 of the Clayton Act (15 U.S.C. § 14). An antitrust complaint must contain "factual allegations . . . enough to raise a right to relief above the speculative level[.]" *Bell Atlantic Corp. v. Twombly*, 127 S.Ct. 1955, 1965 (2007). The Complaint fails to state a claim upon which relief can be granted for the following reasons, among others:

1. Plaintiff has failed to plead an anticompetitive effect in a market for a second, or tied, product.

a. Plaintiff has failed to plead a relevant market in which the tied products compete. *Cascade Health Solutions v. PeaceHealth*, 515 F.3d 883, 912 (9th Cir. 2008); *Catch Curve, Inc. v. Venali, Inc.*, 519 F. Supp. 2d 1028, 1039 (C.D. Cal. 2007).

b. Plaintiff has failed to plead that as a result of Defendants' conduct, competition in a second, tied product market was reduced and that the reduction in competition in that market harmed Plaintiff. *Illinois Tool Works Inc. v. Indep. Ink, Inc.*, 547 U.S. 28, 34 (2006); *Siegel v. Chicken Delight, Inc.*, 448 F.2d 43, 47 (9th Cir. 1971); *In re eBay Seller Antitrust Litig.*, 545 F. Supp. 2d 1027, 1033-34 (N.D. Cal. 2008).

2. Plaintiff has failed to allege that Defendants have market power in a relevant product market for the tying product. *Rick-Mik Enterprises. Inc. v. Equilon Enterprises, LLC*, No. 06-55937, 2008 U.S. App. LEXIS 14761, at *18 (9th Cir. July 11, 2008). Further, Plaintiff has failed to plead that there are barriers to entry or expansion in the market for the tying product. Without barriers to entry in the market for the tying product, Defendants cannot possess market

power. *W. Parcel Expr. v. United Parcel Serv. of Am.*, 190 F.3d 974, 975 (9th Cir. 1999). In fact, Plaintiff has pled that major toy companies have freely entered the market in competition with Defendants, which contradicts Plaintiff's allegation of market power.

Therefore, after consideration of the briefs and arguments of counsel and all other matters presented to the Court, and good cause appearing therefore, IT IS HEREBY ORDERED that:

1. Defendants Ganz, Inc.'s and Ganz U.S.A., LLC's Motion to Dismiss is granted; and

2. This action is dismissed with prejudice.

DATED: _____

_____
HONORABLE JEFFREY S. WHITE
UNITED STATES DISTRICT COURT JUDGE

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